What if there is no Brexit deal

Indirect Tax **Tax voice**

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Tarlochan Lall considers the main consequences for VAT

The paper issued by the Government on 23 August 2018 seeks to provide guidance for ‘UK businesses of the implications for VAT rules for goods and services trade between the UK and EU member states’. The paper is confined to cross border trade and does not deal with the VAT rules that will apply to domestic trade.

It confirms that

- The UK will continue to have a VAT system after it leaves the EU. … The VAT rules relating to UK domestic transactions will continue to apply to businesses as they do now.
- Current rules for imports from non-EU countries will also apply to imports from the EU.
- There will be some specific changes to the VAT rules and procedures that apply to transactions between the UK and EU member states.

It said that there will be ‘VAT changes that businesses will need to prepare for when importing goods from the EU’. It should be obvious to advisers that VAT and customs duties will be payable but many businesses, especially small businesses, may not appreciate that and it would have been helpful to make it clearer in the paper.

VAT accounting for imports

The most significant change announced is that

> “the government will introduce postponed accounting for import VAT on goods brought into the UK.”

Businesses importing goods to the ‘UK will be able to account for import VAT on their VAT return, rather than paying import VAT on or soon after the time that the goods arrive at the UK border’ and that this is to ‘mitigate any adverse cash-flow impacts’ they would otherwise have had if required to pay VAT before having goods released at borders.

The paper does not deal with how input tax claims will work. It is not made clear whether something akin to the reverse charge mechanism for EU acquisitions will be introduced. Currently, VAT on non-EU imports can only be claimed once HMRC issue a form C79 or give permission for input tax to be estimated where the mechanism for issuing form C79 is likely to cause the business difficulty. Subject to clarification on that, the cash-flow impact would only be delayed because the VAT will have to be accounted for through the VAT returns and if input tax cannot be claimed on that VAT return, there would be a real VAT cost. Businesses which only make taxable supplies and can recover their VAT in full may experience limited cash-flow impact. However, correct VAT accounting will be required as errors may lead to interest and penalties. Exempt, partially exempt businesses and importers who cannot recover their VAT in full will have a real VAT cost on their imports. They will also have to pay any customs duties; and VAT will also be due on top of those customs duties.

Perhaps more surprising was the announcement that postponed VAT accounting is to apply to non-EU imports as well, although again, customs duties would apply. The paper states that:

> "To ensure equity of treatment, in a no deal scenario, businesses importing goods will be able to account for their import VAT from non-EU countries in the same way, which will help UK businesses make the most of trading opportunities around the world. Customs declarations and the payment of any other duties will still be required."

The start of that paragraph indicates that the Government may have accepted that it is obliged by the principle of non-discrimination under the rules of the World Trade Organisation (WTO) to extend equal treatment to non-EU imports. Essentially, unilateral favorable treatment of EU imports must be extended to all WTO members. However, the paper does not make reference to the WTO rules. Alternatively, it may be a policy decision to encourage international trade and extend the cash-flow benefit to imports coming into the UK. If this measure recognises the obligation to give equal treatment under WTO rules, it may set a precedent for other relieving measures which may be unilaterally introduced under the Taxation (Cross-border Trade) Bill.

A sting in the tail?

Although these measures will be welcomed by businesses, they carry risks. The EC recognised in its paper 'On an action plan on VAT' COM (2016) 148 that essentially, not having to account for VAT at borders has been "the root cause of cross-border fraud", known as missing trader fraud. Although importers have to account for VAT on EU acquisitions, and they will have to on EU and non-EU imports, fraudulent traders fail to do so and disappear. The Taxation (Cross-border Trade) Bill specifically retains the Kittel principle under which businesses, even if they do not know about the fraud, can lose the input tax on their purchases where they should have known about the fraud. Although a business can escape liability by demonstrating that they took all reasonable measures to avoid entering into their transactions connected with fraud, an increasing number of cases show that it can be extremely difficult to rely on that let out. Seemingly welcome relaxations may come to haunt businesses unknowingly caught in fraud in their supply chains.

Mail order trading and the like

Increasing amounts of internet purchases mean that announcements concerning goods purchased overseas are important.

The paper declares that ‘VAT will be payable on goods entering the UK as parcels sent by overseas businesses’. The government had stated in the Customs Bill White Paper (published in October 2017) ‘that Low Value Consignment Relief (LVCR) will not be extended to goods entering the UK from the EU’ in order to protect UK high street businesses suffering a competitive disadvantage on their sales of goods valued £15 or less being subject to VAT yet those coming from the EU not. The competitive advantage for goods coming from the Channel Islands was removed in 2012. LVCR currently remains for goods coming from other non-EU countries, although the EU proposed its abolition throughout the EU in December 2017 as part of its ‘Modernising VAT for e-commerce’ initiative.

There are separate proposals for goods valued up to £135 or above that amount.

Goods valued up to £135

VAT on parcels sent by suppliers valued up to £135 will be due from the supplier, who will charge UK VAT, register in the UK and account for the VAT. There will be no VAT registration threshold, as is the case for non-established businesses now. The VAT registration process is to be facilitated by a ‘technology based solution’. The supplier will be able to register online and acquire a Unique Identifier, which must accompany the parcels they send to the UK. The online registration will be available from early 2019 so businesses can familiarise themselves with the new obligations. The power to introduce regulations concerning postal packets was included in the first draft of the Taxation (Cross-border Trade) Bill. This approach is also aimed at relieving the burden on the Royal Mail and parcel operators otherwise responsible for collecting the VAT. The £135 threshold is aligned to the current threshold below which no customs duties are due on non-EU imports except in the case for excise goods, i.e. alcohol, tobacco or tobacco products and toilet waters.

Distance selling rules will no longer apply to EU suppliers selling goods to consumers in the UK.

Goods valued above £135

VAT and customs duties on parcels of goods sent to UK customers will ‘continue to be collected from UK recipients in line with current procedures for parcels from non-EU countries’. Parcels of such goods must be accompanied by an accurate and full declaration (forms CN22 or CN23). The sender is not responsible for the VAT or duties. The recipient of the parcel must pay the VAT and duties (including excise duties where applicable), together with handling charges, and the carrier delivering the goods is responsible for the VAT and duties, so must collect them from the recipient. As mentioned above, the £135 threshold seeks to relieve the burden that would otherwise arise on such carriers in the absence of the threshold. Although currently, non-EU parcels valued at above £15 are subject to VAT, which must be accounted for by the carrier, the volume of parcels from the EU is expected to be much higher.

There appears to be a warning that parcel carriers and customers may have exposure to VAT “potentially in cases where their supplier is not compliant with HMRC’ new parcels policy”, which suggests that where a supplier of parcels valued below £135 does not register and account for VAT, the carrier and customer may be liable. HMRC is working with “relevant industry stakeholders” and further information will be provided in due courses.

Other important matters

There are a number of specific issues that should be noted:

- **Exports to the EU**: UK business exporting to the EU ‘may need to plan for customs and VAT processes, which will be checked at the EU border’.
- **Business to Consumer (B2C)**: In the case of B2C supplies, as distance selling rules will no longer apply to EU/UK trade, although the exports will be zero rated, there are traps for UK businesses. Under current EU rules, the UK business could be liable for the import VAT and customs duties when the goods enter the EU, which is mentioned in the paper, and also be liable for registering and accounting for VAT in the EU member states, not mentioned in the paper.
- **Business to Business (B2B)**: In the case of B2B supplies, once again the sales will be zero rated in the UK and the supplier will need to retain evidence of exports currently required for non-EU exports, but no EC sales lists will need to be completed. The business customer will be importing goods into the EU and they will be subject to local VAT and customs duties both of which “may be due at the border”. The UK supplier should check its commercial contract to

establish who is responsible for any VAT and customs due at the border and may need to take local advice as well and require a local fiscal representative Additional costs may have an impact on their EU sales.

- **Supplies by UK business in the EU of goods stored in EU member states**: these will require local VAT registrations under current EU VAT rules.
- **Supplies of services into the EU**: "the main VAT 'place of supply' rules will remain the same for UK businesses" and will "continue to apply in broadly the same way that they do now". The potential change "flagged" is that entitlement to deduction of input tax in connection with supplies of insurance and financial services to the EU may be changed, with an update to follow. In the case of digital B2C supplies of services, VAT will be due in the MS where the customer is resident so they will require an EU registration.
- **MOSS (mini-one-stop-shop)**: UK businesses will have to register for the MOSS non-union scheme in one of the EU member states. Such registrations can only be done once the UK leaves the EU and businesses will have 10 days to register. Businesses should nevertheless take steps to secure such a registration. The EU's extension of MOSS for small enterprises as part of its 'Modernising VAT for e-commerce' initiative is unlikely to be available to UK businesses following Brexit.
- **EU VAT refunds**: UK businesses will no longer have access to the EU refund system and will have to use the processes for non-EU businesses. In essence, businesses are likely to experience delays in securing refunds especially as the volume of claims are likely to rise for local VAT administrations in the EU.
- **Northern Ireland**: businesses affected are advised to 'consider whether they need advice from the Irish government' on what preparations they should make as the Irish government needs to discuss arrangements needed in the event of a new deal with the European Commission.
- **Vehicles imported into the UK**: import VAT will be due on vehicles brought into the UK from the EU. Businesses importing vehicles can use the Notification of Vehicle Arrival Procedure (NOVA) to ensure that the VAT due is paid. DVLA will not register vehicles without a valid NOVA notification.
- **TOMS**: the UK will leave this EU scheme for tour operators. HMRC is working with the travel industry to "minimise any impact".
- **VIES**: this is another EU scheme under which the VAT numbers of EU businesses can continue to be checked by UK businesses but UK VAT registration numbers will no longer be part of the scheme. HMRC is developing an alternative system for UK VAT numbers. This will increase due diligence

requirements for UK businesses with exposure for inadequate due diligence.

Conclusion

The approach of essentially listing areas which require further enquiry mirrors the approach in the paper. Readers are left to work out the details and many businesses will require professional advice. The Financial Times reported that the Federation of Small Businesses complained that this series of papers are “too technical for most businesses to “make head nor tail of”” and they are being forced to incur costs of professional advice.